UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF TEXAS
LUFKIN DIVISION

UNITED STATES OF AMERICA, ex rel. J. BENJAMIN JOHNSON, JR., et al., Plaintiffs, v. SHELL OIL COMPANY, et al. Defendants.	C.A. NO. 9:96CV66 JUDGE HANNAH

UNITED STATES' RESPONSE TO DEFENDANTS' MOTION TO DISMISS FOR LACK OF SUBJECT MATTER JURISDICTION OR ON PRIMARY JURISDICTION GROUNDS

The United States hereby opposes the motion to dismiss of defendants Texaco, Inc., Texaco Oil & Trading Supply Co., Texaco Trading & Transportation, Inc., Texaco Producing, Inc., Texaco Refining & Marketing, Inc., Four Star Oil & Gas Co.

For the reasons set out in the accompanying memorandum of points and authorities, the United States hereby requests that the Court deny defendants' motion to dismiss the government's complaint for lack of subject matter jurisdiction or, in the alternative, on primary jurisdiction grounds.

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Respectfully submitted,

STUART E. SCHIFFER
Deputy Assistant Attorney General

MIKE BRADFORD
United States Attorney
Eastern District of Texas

O. Kenneth Dodd * by permission by Alida Parker
O. KENNETH DODD
Texas Bar No. 05931685
Assistant U.S. Attorney
350 Magnolia Street, Suite 150
Beaumont, TX 77701
Ph: (409) 839-2538
Fax: (409) 839-2538
ATTORNEY IN CHARGE

Dodge Wells * by permission by Alida Parker
JOYCE R. BRANDA
ALAN E. KLEINBURD

DODGE WELLS
District of Columbia Bar No. 425194
ATTORNEY IN CHARGE

PATRICIA R. DAVIS
RINA TUCKER
TOM LEDERMAN
ROBERT MCAULIFFE
Attorneys
Commercial Litigation Branch
Civil Division
U.S. Department of Justice
P.O. Box 261
Ben Franklin Station
Washington, D.C. 20044
Ph: (202) 307-0407
Fax: (202) 514-7361

Dated: August 14, 1998

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing United States' Response to Defendants' Motion to Dismiss and Supporting Memorandum were served by United States mail on the 14th day of August, 1998, on counsel of record in this case.

O. Kenneth Dodd * by permission by Andrea Parker

O. KENNETH DODD

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MEMORANDUM OF THE UNITED STATES OPPOSING MOTION AND MEMORANDUM OF THE TEXACO DEFENDANTS TO DISMISS FOR LACK OF SUBJECT MATTER JURISDICTION OR ON PRIMARY JURISDICTION GROUNDS

The Texaco defendants ("Texaco") have moved to dismiss the complaint filed by the United States on the grounds that the government has elected to pursue its False Claims Act claims through the administrative process. Texaco's motion, while creative, is devoid of factual support or legal merit and should be denied.

Texaco points out that after the relators filed their initial complaints under seal and before the United States intervened in this case, the Minerals Management Service ("MMS") of the Department of the Interior conducted audits of Texaco and issued two orders to pay additional royalties for oil produced in California. Motion and Memorandum to Dismiss The Relators' Second Consolidated Complaint and the Complaint of the United States for Lack of Subject

Matter Jurisdiction, or, in the Alternative, on Primary Jurisdiction Grounds (Texaco memo") at 12-15. Texaco asserts that the orders to pay contain the same allegations concerning underpayment of royalties by Texaco as are stated in the Government's complaint in this case. Id. at 14, 15.[1/] Texaco further asserts that the orders to pay constitute an election by the Government, pursuant to 31 U.S.C.§ 3730(c)(5) to pursue its claims for Texaco's knowing underpayment of royalties through the administrative process.

Section 3730(c)(5) states, in relevant part:

> [t]he Government may elect to pursue its claim through any alternative remedy available to the Government, including any administrative proceeding to determine a civil monetary penalty. If any such alternate remedy is pursued in another proceeding, the person initiating the action shall have the same rights in such proceeding as such person would have had if the action had continued under this section.

Texaco's argument suffers from numerous fatal deficiencies. First, the orders to pay do not expose Texaco to civil monetary penalties, as that term is used in § 3730(c)(5), for underpayment of royalties. Second, in the view of the Department of the Interior, an order to pay is not a "claim," and therefore issuance of orders to pay to Texaco cannot represent a decision by the Government to pursue its False Claims Act claim through an alternative remedy. Third, an MMS audit and a resulting order to pay is not an "administrative proceeding." Fourth, § 3730(c)(5) requires an explicit election by the Government to pursue an administrative remedy. Fifth, MMS

[1/] Texaco's ability to analyze the Government's complaint refutes Texaco's claims, in support of its motion to dismiss the complaint pursuant to Rule 9(b), that "the Texaco defendants cannot reasonably formulate a responsive pleading" to the complaint, Motion and Memorandum to Dismiss the Complaint of the United States of America Pursuant to Rules 9(b) and 12(b)(6) at 3, and that it is "virtually impossible for Texaco to make an informed response" to the complaint, Id. at 13.

have authority to make an election pursuant to § 3730(c)(5) to elect an alternative remedy.

Section 3730(c)(5) was added to the False Claims Act in 1986. The Senate Report on the 1986 amendments stated that the new provision:

> [c]larifies that the Government, once it intervenes and takes over a false claim suit brought by a private individual, may elect to pursue any alternative remedy for recovery of the false claim which might be available under the administrative process.

S. Rep 99-345 at 27 (1986), reprinted in 1986 U.S.C.C.A.N. 5266, 5292.[2/] The orders to pay, which are exhibits 5 and 6 to Texaco's memo, do not assert that Texaco knowingly underpaid royalties and do not purport to seek civil monetary penalties as remedies for recovery of false claims. In fact, the orders to pay do not seek civil monetary penalties for any reason. The Federal Oil and Gas Royalty Management Act of 1982 ("FOGRMA"), 30 U.S.C. § 1701 et seq., authorized the Department of Interior to assess civil penalties upon providing notice and a right to hearing. 30 U.S.C. § 1719. The regulations implementing the civil penalty provisions of § 1719 are set forth at 30 CFR § 241.51, which is referenced in both the orders to pay. Civil penalty proceedings are initiated by a "notice of noncompliance," 30 CFR § 241.51(a),(c). MMS is to issue a "penalty notice" "to any person subject to penalties under this section." 30 CFR § 241.51(a). MMS has not issued to Texaco notices of noncompliance or penalty notices for underpayment of royalties.

The Department of Interior has also promulgated regulations, 43 CFR Part 35, implementing administrative remedies for fraudulent claims or statement, as authorized by the

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[2/] The Senate Report's discussion of what was enacted as § 3730(c)(5) is Exhibit 1 to this memorandum.

Programs Fraud Civil Remedies Act of 1986 ("PFCRA"), 31 U.S.C. § 3801 et seq.[3/] The regulations provide that administrative proceedings for fraudulent claims are initiated by a complaint, which may not be issued without written approval by the Department of Justice. 43 CFR § 35.6, 35.7. No such complaint against Texaco has been authorized by the Department of Justice or issued by the Department of the Interior.

Texaco argues that the orders to pay seek statutory interest on royalty underpayments and that the interest charges constitute civil monetary penalties. Texaco memo at 7-8, 14-15. Texaco's argument rests on a paragraph in the House Report on FOGRMA which uses the term "interest penalty" as a synonym for "interest charge."[4/] The statute itself distinguishes between "civil penalties, " which the Department is authorized by 30 U.S.C. § 1719 to assess, for specific violations, after notice and an opportunity for hearing, and "interest charges," which are required by 30 U.S.C. § 1721 to be charged on underpayments or late payments of royalties (and which the

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[3/] The Senate Report on the 1986 amendments to the False Claims Act specifically reference administrative proceedings pursuant to PFCRA as the type of alternative proceedings authorized by 31 U.S.C. § 3730(c)(5).

[4/] Contrary to Texaco's implication, the House Report uses the term "interest penalty" to refer to any interest charge, not as specifically referring to interest charges at the Internal Revenue Service rate:

> Section 116 - Interest Charges
> This section established interest penalties for late payments in the cases where royalty payments are not received by the Secretary on the date that such payments are due and when the Secretary fails to make payment to a State or Indian tribe on the date required. The interest penalty so charged is at the rate applicable under section 6621 of the Internal Revenue Code of 1954. . . .

H.R. Rep. No. 97-859 at 36, reprinted in 1982 U.S.C.C.A.N. 4268, 4290.

Department must pay on any underpayments or late payments to States). In any event, the important issue is not what Congress thought it was doing in enacting FOGRMA, but what Congress intended in enacting 31 U.S.C. § 3730(c)(5). Texaco has provided no support for its apparent position that Congress intended to include a routine audit or review which potentially might result in assessment of interest charges as an administrative proceeding to determine a civil monetary penalty.

Moreover, as Texaco's co-defendants have pointed out, the Department of the Interior does not consider an order to pay to constitute a claim by the agency. See Motion and Memorandum to Dismiss Under Rule 12(b)(6) on Primary Jurisdiction Grounds, filed May 18, 1998 at 8, and Exhibit F thereto. Since the Department does not consider the orders to pay claims against Texaco, the orders cannot constitute an election to pursue the government's claims in this case through administrative proceedings. Further, the audit and resulting orders to pay are not "administrative proceedings" as that term is used in § 3730(c)(5). The one case cited by Texaco which considered §3730(c)(5), United States ex rel. Dunleavy v. County of Delaware, 123 F.3d 734 (3rd Cir. 1997), expressed doubt that an audit and a resulting demand for payment amounted to the type of alternate proceeding contemplated by the section. 123 F.3d at 739, n.8.[5/] The court's doubt is well taken. The Administrative Procedures Act defines an "agency proceeding" as a rule making, an adjudication, or a licensing proceeding. 5 U.S.C. § 551(12). An audit is in none of these categories. An agency should not have to choose between conducting normal audit and oversight activities on one hand or preserving its rights under the False Claims Act on the other hand.

[5/] The court determined for other reasons that the section was inapplicable.

As both the legislative history to § 3730(c)(5), Exhibit 1 to this memorandum, and United States ex rel. Dunleavy v. County of Delaware, 123 F.3d 734, 739 (3rd Cir. 1997), make clear, the section does not apply unless the Government makes an explicit election to pursue an alternative remedy. That election must be made by the Department of Justice. As we argued in the government's response to the motion by Texaco's co-defendants to dismiss on primary jurisdiction grounds, federal agencies, including Interior, are specifically prohibited, by statute, from adjudicating or compromising civil fraud claims. See United States' Memorandum Opposing Defendant's Motion and Memorandum to Dismiss under Rule 12(b)(6) on Primary Jurisdiction Grounds at 3. Texaco does not assert that the Department of Justice has elected an alternative remedy after intervention. For all of these reasons, Texaco's motion must be denied.

Texaco also adopts and joins in the Motion and Memorandum to Dismiss Under Rule 12(b)(6) on Primary Jurisdiction Grounds, filed May 18, 1998 by its co-defendants. On July 23, 1998, the Court entered an order denying the primary jurisdiction motion filed by Texaco's co-defendants, and that order is the law of the case. If any response is necessary, the United States stands on the United States' Memorandum Opposing Defendant's Motion and Memorandum to Dismiss under Rule 12(b)(6) on Primary Jurisdiction Grounds.

Respectfully submitted,

STUART E. SCHIFFER
Deputy Assistant Attorney General

MIKE BRADFORD
United States Attorney
Eastern District of Texas

O. Kenneth Dodd * by permission by Audra Parker

O. KENNETH DODD
Texas Bar No. 05931685
Assistant U.S. Attorney
350 Magnolia Street, Suite 150
Beaumont, TX 77701
Ph: (409) 839-2538
Fax: (409) 839-2538
ATTORNEY IN CHARGE

Dodge Wells * by permission by Audra Parker

JOYCE R. BRANDA
ALAN E. KLEINBURD

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District of Columbia Bar No. 425194
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PATRICIA R. DAVIS
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TOM LEDERMAN
ROBERT MCAULIFFE
Attorneys
Commercial Litigation Branch
Civil Division
U.S. Department of Justice
P.O. Box 261
Ben Franklin Station
Washington, D.C. 20044
Ph: (202) 307-0407
Fax: (202) 514-7361

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EXHIBIT 1

LEGISLATIVE HISTORY
P.L. 99-562

FALSE CLAIMS AMENDMENTS ACT OF 1986

P.L. 99-562, see page 100 Stat. 3153

DATES OF CONSIDERATION AND PASSAGE

Senate August 11, October 3, 1986

House September 9, October 7, 1986

Senate Report (Judiciary Committee) No. 99-345,
July 28, 1986 [To accompany S. 1562]

House Report (Judiciary Committee) No. 99-660,
June 26, 1986 [To accompany H.R. 4827]

Cong. Record Vol. 132 (1986)

The Senate bill was passed in lieu of the House bill. The Senate Report is set out below.

SENATE REPORT NO. 99-345

[page 1]

The Committee on the Judiciary, to which was referred the bill (S. 1562) to amend the False Claims Act, and title 18 of the United States Code regarding penalties for false claims, and for other purposes, having considered the same, reports favorably thereon with an amendment in the nature of a substitute and recommends that the bill, as amended, do pass.

* * * * *

I. PURPOSE OF THE BILL

The purpose of S. 1562, the False Claims Reform Act, is to enhance the Government's ability to recover losses sustained as a result of fraud against the Government. While it may be difficult to estimate the exact magnitude of fraud in Federal programs and

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procurement, the recent proliferation of cases among some of the largest Government contractors indicates that the problem is severe. This growing pervasiveness of fraud necessitates modernization of the Government's primary litigative tool for combatting fraud; the False Claims Act (31 U.S.C. 3729, 3730). The main portions of the act have not been amended in any substantial respect since signed into law in 1863. In order to make the statute a more useful tool against fraud in modern times, the Committee believes the statute should be amended in several significant respects.

The proposed legislation seeks not only to provide the Government's law enforcers with more effective tools, but to encourage

situations where new and significant evidence is found and the Government can show "good cause" for intervening, paragraph (2) provides that the court may allow the Government to take over the suit. Upon request, the Government may also be served with copies of all pleadings and depositions associated with any *qui tam* action it declines to take over.

Subsection (c)(3) of section 3730 clarifies that the Government, once it intervenes and takes over a false claim suit brought by a private individual, may elect to pursue any alternate remedy for recovery of the false claim which might be available under the administrative process. The Department of Health and Human Services is currently authorized to use administrative proceedings for the recovery of some false claims. Earlier in this Congress, the Senate Governmental Affairs Committee favorably reported S. 1134, the Program Fraud Civil Penalties Act, which would extend this type of administrative mechanism for addressing false claims to all Executive agencies. The Committee intends that if civil monetary penalty proceedings are available, the Government may elect to pursue the claim either judicially or through an administrative civil penalty proceeding. In the event that the Government chooses to proceed administratively, the *qui tam* relator retains all the same rights to copies of filings and depositions, to objections of settlements or dismissals, to taking over the action if the Government fails to proceed with "reasonable diligence", as well as to receiving a portion of any recovery. If the Government proceeds administratively, the district court shall stay the civil action pending the administrative proceeding and any petitions by the relator, in order to exercise his rights, will be to the district court. While the Government will have the opportunity to elect its remedy, it will not have an opportunity for dual recovery on the same claim or claims. In other words, the Government must elect to pursue the false claims action either judicially or administratively and if the Government declines to intervene in a *qui tam* action, it is estopped from pursuing the same action administratively or in a separate judicial action.

31 U.S.C. 3730, SUBSECTION (d)

Subsection (d) of section 3730 delineates the *qui tam* relator's right to a portion of any recovery resulting from a successful false claims suit initiated by the relator.

Subsection (d)(1) provides that when the Government has intervened, taken over the suit, and produced a recovery either through a settlement agreement or a judgment, the relator will receive between 10 and 20 percent of the recovery.

Subsection (d)(2) provides that if the relator has litigated the false claims action successfully and the Government did not take over the suit, the relator will be awarded between 20 and 30 percent of the judgment or settlement proceeds.

Current law allows relator awards of up to 10 percent in suits the Government takes over, and up to 25 percent where the relator litigates without the Government. The new percentages found in subsection (d) (1) and (2) do not substantially increase the possible recovery available to a *qui tam* relator, but do create a guarantee